UNITRIN INC
Form 10-K
February 03, 2011

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2010

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
Commission file number: 001-18298

UNITRIN, INC.

(Exact name of registrant as specified in its charter)

Delaware	**95-4255452**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

One East Wacker Drive, Chicago, Illinois **60601**
(Address of principal executive offices) **(Zip Code)**
(312) 661-4600

(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $0.10 par value per share	New York Stock Exchange
Preferred Share Purchase Rights pursuant to Rights Agreement	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes ¨ No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨ Smaller Reporting Company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

As of June 30, 2010, the aggregate market value of the registrant s common stock held by non-affiliates of the registrant was $1.5 billion based on the closing sale price as reported on the New York Stock Exchange. Solely for purposes of this calculation, all executive officers and directors of the registrant are considered affiliates.

Registrant had 61,066,587 shares of common stock outstanding as of January 31, 2011.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held on May 4, 2011 are incorporated by reference into Part III.

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Caution Regarding Forward-Looking Statements

This 2010 Annual Report on Form 10-K (the 2010 Annual Report), including the accompanying consolidated financial statements of Unitrin, Inc. (Unitrin) and its subsidiaries (individually and collectively referred to herein as the Company) and the notes thereto appearing in Item 8 herein (the Consolidated Financial Statements), the Management s Discussion and Analysis of Financial Condition and Results of Operations appearing in Item 7 herein (the MD&A) and the other Exhibits and Financial Statement Schedules filed as a part hereof or incorporated by reference herein may contain or incorporate by reference information that includes or is based on forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements give expectations or forecasts of future events. The reader can identify these statements by the fact that they do not relate strictly to historical or current facts. They use words such as believe(s), goal(s), target(s), estimate(s), anticipate(s), forecast(s), project(s), plan(s), intend might, may and other words and terms of similar meaning in connection with a discussion of future operating, financial performance or financial condition. Forward-looking statements, in particular, include statements relating to future actions, prospective services or products, future performance or results of current and anticipated services or products, sales efforts, expenses, the outcome of contingencies such as legal proceedings, trends in operations and financial results.

Any or all forward-looking statements may turn out to be wrong, and, accordingly, readers are cautioned not to place undue reliance on such statements, which speak only as of the date of this 2010 Annual Report. These statements are based on current expectations and the current economic environment. They involve a number of risks and uncertainties that are difficult to predict. These statements are not guarantees of future performance; actual results could differ materially from those expressed or implied in the forward-looking statements. Forward-looking statements can be affected by inaccurate assumptions or by known or unknown risks and uncertainties. Many such factors will be important in determining the Company s actual future results and financial condition. The reader should consider the following list of general factors that could affect the Company s future results and financial condition, as well as those discussed below under Item 1A., Risk Factors , in this 2010 Annual Report.

Among the general factors that could cause actual results and financial condition to differ materially from estimated results and financial condition are:

- The incidence, frequency, and severity of catastrophes occurring in any particular reporting period or geographic concentration, including natural disasters, pandemics and terrorist attacks or other man-made events;

- The number and severity of insurance claims (including those associated with catastrophe losses) and their impact on the adequacy of loss reserves;

- Changes in facts and circumstances affecting assumptions used in determining loss and LAE reserves;

- The impact of inflation on insurance claims, including, but not limited to, the effects attributed to scarcity of resources available to rebuild damaged structures, including labor and materials and the amount of salvage value recovered for damaged property;

- Changes in the pricing or availability of reinsurance, or in the financial condition of reinsurers and amounts recoverable therefrom;

- Orders, interpretations or other actions by regulators that impact the reporting, adjustment and payment of claims;

- The impact of residual market assessments and assessments for insurance industry insolvencies;

- Changes in industry trends and significant industry developments;

Uncertainties related to regulatory approval of insurance rates, policy forms, license applications and similar matters;

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Developments related to insurance policy claims and coverage issues, including, but not limited to, interpretations or decisions by courts or regulators that may govern or influence such issues arising with respect to losses incurred in connection with hurricanes and other catastrophes;

Changes in ratings by credit rating agencies, including A.M. Best Co., Inc. (A.M. Best);

Adverse outcomes in litigation or other legal or regulatory proceedings involving Unitrin or its subsidiaries or affiliates;

Regulatory, accounting or tax changes that may affect the cost of, or demand for, the Company s products or services;

Governmental actions, including, but not limited to, implementation of the provisions of the Patient Protection and Affordable Care Act, the Health Care and Education Reconciliation Act of 2010 and the Dodd-Frank Act, new laws or regulations or court decisions interpreting existing laws and regulations or policy provisions;

Changes in distribution channels, methods or costs resulting from changes in laws or regulations, lawsuits or market forces;

Changes in laws or regulations governing or affecting the regulatory status of industrial banks, such as Fireside Bank, and their parent companies, including minimum capital requirements and restrictions on the non-financial activities and equity investments of companies that acquire control of industrial banks;

Changes in the estimated rates of automobile loan receivables net charge-off used to estimate Fireside Bank s reserve for loan losses, including, but not limited to, changes in general economic conditions, unemployment rates and the impact of changes in the value of collateral held;

The degree of success in effecting an orderly wind-down of the operations of Fireside Bank and the recovery of Unitrin s investment in Fireside Bank;

Changes in general economic conditions, including performance of financial markets, interest rates, unemployment rates and fluctuating values of particular investments held by the Company;

The level of success and costs expended in realizing economies of scale and implementing significant business consolidations and technology initiatives;

Heightened competition, including, with respect to pricing, entry of new competitors and the development of new products by new and existing competitors;

Increased costs and risks related to data security;

Absolute and relative performance of the Company s products or services; and

Other risks and uncertainties described from time to time in Unitrin s filings with the U.S. Securities and Exchange Commission (SEC).

No assurances can be given that the results contemplated in any forward-looking statements will be achieved or will be achieved in any particular timetable. The Company assumes no obligation to publicly correct or update any forward-looking statements as a result of events or developments subsequent to the date of this 2010 Annual Report. The reader is advised, however, to consult any further disclosures Unitrin makes on related subjects in its filings with the SEC.

PART I

Item 1. Business.

Unitrin, incorporated in Delaware in 1990, is a diversified insurance holding company, with subsidiaries that principally provide life, automobile, homeowners and other insurance products for individuals and small businesses.

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Unitrin s annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments thereto are accessible free of charge through Unitrin s website, unitrin.com, as soon as reasonably practicable after such materials are filed with or furnished to the SEC.

(a) GENERAL DEVELOPMENT OF BUSINESS

Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010

During the first quarter of 2010, the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 (the Health Care Acts) were signed into law. The business model of Reserve National Insurance Company (Reserve National), which focuses on providing limited health insurance coverages to persons who lack access to traditional private options, is likely to be adversely affected by the implementation of the Health Care Acts. Reserve National might suffer significant loss of revenue and might not be able to compete effectively in the markets that it has historically served. Certain provisions that establish minimum loss ratios for health insurance policies significantly above the levels historically experienced by Reserve National could adversely impact Reserve National s ability to achieve an adequate return and may result in a significant loss of business for Reserve National. A significant loss of business could have a material adverse effect on the financial condition and results of operations of Reserve National. In the third quarter of 2010, the Company determined that the goodwill associated with Reserve National was impaired and not recoverable and wrote off $14.8 million of goodwill.

See MD&A, Life and Health Insurance, Note 7, Goodwill, to the Consolidated Financial Statements, Regulation under this Item 1 beginning on page 20 and Item 1A., Risk Factors, under the caption Reserve National s business model is vulnerable to American health care reform.

Purchase of Kemper Name

On June 29, 2010, Unitrin purchased all rights to the Kemper name owned by Lumbermens Mutual Casualty Company and its affiliates (Lumbermens). These rights include registered trademarks, logos and internet domain names incorporating the Kemper name. As a result of the transaction, Unitrin has acquired unrestricted use of the Kemper name in connection with all of its operations and Kemper® became a registered service mark of Unitrin. Prior to purchasing the rights, the Company was licensed to use the Kemper name only in connection with the personal lines business. Lumbermens, had for many years owned the intellectual property rights to the Kemper name in the insurance marketplace and had conducted its various insurance businesses under the name Kemper Insurance Companies. Lumbermens has ceased all use of the Kemper name.

Retirement of 2010 Senior Notes and Issuance of 2015 Senior Notes

On November 1, 2010, Unitrin repaid and retired $200 million aggregate principal amount of its 4.875% Senior Notes due November 1, 2010 (the 2010 Senior Notes).

On November 24, 2010, Unitrin issued $250 million aggregate principal amount of its 6.00% Senior Notes due November 30, 2015 (the 2015 Senior Notes) in a public offering. The 2015 Senior Notes are unsecured and may be redeemed in whole at any time or in part from time to time at Unitrin s option at specified redemption prices. Unitrin issued the 2015 Senior Notes for proceeds of $247.8 million, net of transaction costs, for an effective yield of 6.21%. Unitrin used the net proceeds from the offering to repay borrowings of $140 million under its credit facility, to make a capital contribution of $60 million to its subsidiary, United Insurance Company of America (United Insurance), and for working capital and other general corporate purposes.

Unitrin Common Stock Repurchases

During 2010, Unitrin repurchased approximately 1.4 million shares of its common stock at an aggregate cost of $34.4 million in open market transactions. Unitrin s stock repurchase program was first announced on August 8, 1990. The repurchase program was subsequently expanded several times, most recently in November 2006, when

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the Board of Directors expanded Unitrin s authority to repurchase Unitrin s common stock by an aggregate of 6.0 million shares (in addition to approximately 0.8 million shares remaining under its prior authorization). No shares remained available for repurchase under this repurchase program at December 31, 2010.

On February 2, 2011, the Board of Directors approved a new common stock repurchase program. Under the new program, Unitrin is authorized to repurchase up to $300 million worth of its common stock. Repurchases may be made from time to time at prevailing prices in the open market or in privately-negotiated transactions, subject to market conditions and other factors. Repurchases will be financed through Unitrin s general corporate funds. Depending upon the amount of repurchases and other factors, Unitrin may also borrow funds under its existing revolving credit facility.

(b) BUSINESS SEGMENT FINANCIAL DATA

Financial information about Unitrin s business segments for the years ended December 31, 2010, 2009 and 2008 is contained in the following sections of this 2010 Annual Report of Unitrin, Inc. and is incorporated herein by reference: (i) Note 21, Business Segments, to the Consolidated Financial Statements; and (ii) MD&A.

(c) DESCRIPTION OF BUSINESS

Unitrin is a diversified insurance holding company, with subsidiaries that provide automobile, homeowners, life, health, and other insurance products for individuals and small businesses. The Company is engaged, through its subsidiaries, in the property and casualty insurance, life and health insurance and automobile finance businesses. The Company conducts its operations through five operating segments: Kemper, Unitrin Specialty, Unitrin Direct, Life and Health Insurance and Fireside Bank. Fireside Bank s automobile finance business is in runoff.

Unitrin s subsidiaries employ approximately 7,130 full-time associates supporting its operations, of which approximately 870 are employed in the Kemper segment, 710 in the Unitrin Specialty segment, 560 in the Unitrin Direct segment, 430 shared by the Kemper, Unitrin Specialty and Unitrin Direct segments, 3,980 in the Life and Health Insurance segment, 380 at Fireside Bank and the remainder in various corporate and other staff functions.

Property and Casualty Insurance Business

Unitrin s property and casualty insurance business operations are primarily conducted through the Kemper, Unitrin Specialty, and Unitrin Direct segments. In addition, the Life and Health Insurance segment s career agents also sell property insurance to its customers. Unitrin s insurance subsidiaries operating in the Kemper, Unitrin Specialty, Unitrin Direct and Life and Health Insurance segments provide automobile, homeowners, fire, and other types of property and casualty insurance to individuals and commercial automobile insurance to businesses. Automobile insurance in these segments accounted for 56%, 59% and 57% of Unitrin s consolidated insurance premiums earned from continuing operations for the years ended December 31, 2010, 2009 and 2008, respectively. Automobile insurance in these segments accounted for 47%, 49% and 50% of Unitrin s consolidated revenues from continuing operations for the years ended December 31, 2010, 2009 and 2008, respectively. Homeowners insurance in these segments accounted for 13%, 12% and 12% of Unitrin s consolidated insurance premiums earned from continuing operations for the years ended December 31, 2010, 2009 and 2008, respectively. Homeowners insurance in these segments accounted for 11%, 10% and 11% of Unitrin s consolidated revenues from continuing operations for the years ended December 31, 2010, 2009 and 2008, respectively.

Property insurance indemnifies an insured with an interest in physical property for loss of, or damage to, such property or the loss of its income-producing abilities. Casualty insurance primarily covers liability for damage to property of, or injury to, a person or entity other than the insured. In most cases casualty insurance also obligates the insurance company to provide a defense for the insured in litigation arising out of events covered by the policy.

The Kemper and Unitrin Specialty segments distribute their products through independent agents who are paid commissions for their services. The Unitrin Direct segment distributes its products directly to consumers and through employer-sponsored voluntary benefit programs and other affinity relationships.

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Kemper

Kemper, based in Jacksonville, Florida, conducts business in 38 states and the District of Columbia. In 2010, the following states provided over half of the premium revenues included in this segment: New York (19%), California (13%), North Carolina (12%) and Texas (11%).

Kemper primarily sells preferred and standard risk automobile and homeowners insurance. Kemper s insurance products accounted for 51% of the aggregate insurance premium revenues of Unitrin s property and casualty insurance business in 2010. Kemper s products are marketed by approximately 2,600 independent insurance agents. These personal lines products are designed and priced for those individuals who have demonstrated favorable risk characteristics and loss history. Typical customers include middle to upper income individuals and families.

Unitrin Specialty

Unitrin Specialty, based in Dallas, Texas, conducts business in 21 states, principally in the midwest, southeast, southwest and western United States. In 2010, the following states provided more than three-fifths of the premium revenues in this segment: California (44%), Texas (18%), Washington (7%) and Louisiana (4%).

Unitrin Specialty provides nonstandard personal and commercial automobile insurance. Unitrin Specialty s insurance products accounted for 27% of the aggregate insurance premium revenues of Unitrin s property and casualty insurance business in 2010. Nonstandard automobile insurance is provided for individuals and businesses that have had difficulty obtaining standard or preferred risk insurance, usually because of their driving records, claims experience or premium payment history. Unitrin Specialty s products are marketed through approximately 8,000 independent agents and brokers.

Unitrin Direct

Unitrin Direct, based in Chicago, Illinois, markets automobile and homeowners insurance primarily via direct mail, web insurance portals, click-thrus, its own websites, employer-sponsored voluntary benefit programs and other affinity relationships. The Unitrin Direct segment s automobile and homeowners insurance products are available in 48 states and the District of Columbia. In 2010, the following states provided approximately two-thirds of the premium revenues in this segment: Florida (16%), New York (14%), California (10%), Texas (6%), Connecticut (5%), Michigan (5%), Pennsylvania (5%) and Georgia (5%). Unitrin Direct s insurance products accounted for 16% of the aggregate insurance premium revenues of Unitrin s property and casualty insurance business in 2010.

Unitrin Direct writes a broad spectrum of personal automobile insurance risks ranging from preferred to non-standard private passenger automobile insurance risks, and competes with companies that sell insurance directly to the consumer and employer-sponsored voluntary benefit programs, as well as companies that sell through agents. Unitrin Direct also offers homeowners and renters insurance across 48 states and the District of Columbia, complementing its direct automobile insurance business.

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Property and Casualty Loss and Loss Adjustment Expense Reserves

The Company s reserves for losses and loss adjusting expenses (LAE) for property and casualty insurance (Property and Casualty Insurance Reserves) are reported using the Company s estimate of its ultimate liability for losses and LAE for claims that occurred prior to the end of any given accounting period but have not yet been paid. The Company had $1,118.7 million and $1,211.3 million of gross loss and LAE reserves at December 31, 2010 and 2009, respectively. Property and Casualty Insurance Reserves by business segment at December 31, 2010 and 2009 were:

DOLLARS IN MILLIONS	**2010**	**2009**
Business Segments:		
Kemper	**$ 420.5**	$ 422.7
Unitrin Specialty	**250.8**	277.9
Unitrin Direct	**235.6**	247.0
Life and Health Insurance	**20.8**	19.0
Total Business Segments	**927.7**	966.6
Discontinued Operations	**163.9**	214.4
Unallocated Reserves	**27.1**	30.3
Total Property and Casualty Insurance Reserves	**$ 1,118.7**	$ 1,211.3

Certain reserves acquired in connection with a business acquisition from SCOR Reinsurance Company (SCOR) in 2002 (the Unallocated Reserves) are reinsured by an insurance subsidiary of SCOR (see Note 8, Property and Casualty Insurance Reserves, to the Consolidated Financial Statements). The Company does not allocate these reserves to its business segments.

In estimating the Company s Property and Casualty Insurance Reserves, the Company s actuaries exercise professional judgment and must consider, and are influenced by, many variables that are difficult to quantify. Accordingly, the process of estimating and establishing the Company s Property and Casualty Insurance Reserves is inherently uncertain and the actual ultimate net cost of claims may vary materially from the estimated amounts reserved. The reserving process is particularly imprecise for claims involving asbestos, environmental matters, construction defect and other emerging and/or long-tailed exposures that may not be discovered or reported until years after the insurance policy period has ended. Property and Casualty Insurance Reserves related to the Company s Discontinued Operations are predominantly long-tailed exposures, of which $59.8 million was related to asbestos, environmental matters and construction defect exposures at December 31, 2010. See MD&A, Critical Accounting Estimates, under the caption Property and Casualty Insurance Reserves for Losses and Loss Adjustment Expenses beginning on page 71 for a discussion of the Company s reserving process and the factors considered by the Company s actuaries in estimating the Company s Property and Casualty Insurance Reserves.

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The Company s goal is to ensure that its total reserves for property and casualty insurance losses and LAE are adequate to cover all costs, while sustaining minimal variation from the time reserves for losses and LAE are initially estimated until losses and LAE are fully developed. Changes in the Company s estimates of these losses and LAE, also referred to as development, will occur over time and may be material. Favorable development is recognized and reported in the Consolidated Financial Statements when the Company decreases its previous estimate of ultimate losses and LAE and results in an increase in net income in the period recognized, whereas adverse development is recognized and reported in the Consolidated Financial Statements when the Company increases its previous estimate of ultimate losses and LAE and results in a decrease in net income. The Company recognized total favorable development of $24.9 million, $80.9 million and $79.3 million before tax for the years ended December 31, 2010, 2009 and 2008, respectively. Development for each of the Company s continuing business segments and Unitrin Business Insurance for the years ended December 31, 2010, 2009 and 2008 was:

	Favorable (Adverse) Development		
DOLLARS IN MILLIONS	**2010**	**2009**	**2008**
Continuing Operations:			
Kemper	**$ 23.8**	$ 60.5	$ 61.0
Unitrin Specialty	**(4.1)**	7.9	5.5
Unitrin Direct	**6.8**	12.1	(3.2)
Life and Health Insurance	**(4.5)**	(2.6)	(13.7)
Total Favorable Development from Continuing Operations, Net	**22.0**	77.9	49.6
Discontinued Operations:			
Unitrin Business Insurance	**2.9**	3.0	29.7
Total Favorable Development, Net	**$ 24.9**	$ 80.9	$ 79.3

Development in the Company s Kemper segment comprised a substantial portion of the Company s development reported in continuing operations in 2010, 2009 and 2008. See MD&A, Critical Accounting Estimates, under the caption Property and Casualty Insurance Reserves for Losses and Loss Adjustment Expenses Kemper Development for additional information regarding this development. Adverse development in the Life and Health Insurance segment in 2010 and 2008 is due primarily to adverse development on certain hurricanes. See MD&A, Catastrophes and Life and Health Insurance, and Note 25, Contingencies, to the Consolidated Financial Statements for additional information on the impact of catastrophes on the development reported for the Company s Life and Health Insurance segment. See MD&A, Catastrophes, Kemper, Unitrin Specialty, Unitrin Direct, and Life and Health Insurance for the impact of development on the results reported by the Company s business segments.

Development in Unitrin Business Insurance comprised all of the Company s development reported in discontinued operations. On June 3, 2008, the Company sold its Unitrin Business Insurance operations to AmTrust Financial Services, Inc. (AmTrust). The Company retained Property and Casualty Insurance Reserves for unpaid insured losses that occurred prior to June 1, 2008, the effective date of the sale. Development for Unitrin Business Insurance in 2010 and 2009 did not have as great of an impact, as compared to 2008, as the losses and LAE became more fully developed. The impact of development, either favorable or adverse, should decline over time as the losses and LAE continue to be more fully developed.

See Note 8, Property and Casualty Insurance Reserves to the Consolidated Financial Statements for a tabular reconciliation for the three most recent annual periods setting forth the Company s Property and Casualty Insurance Reserves as of the beginning of each year, incurred losses and LAE for insured events of the current year, changes in incurred losses and LAE for insured events of prior years, payments of losses and LAE for insured events of the current year, payments of losses and LAE for insured events of prior years and the Company s Property and Casualty Insurance Reserves at the end of the year and additional information regarding the nature of adjustments to incurred losses and LAE for insured events of prior years.

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Ten Year Loss Development History

The following table illustrates the changes over time in the Company s estimate of reserves for losses and LAE. The first section shows the amount of reserves reported in the Company s consolidated financial statements as originally reported at the end of each calendar year. The second section, reading down, shows the cumulative amount of payments made through the end of each successive year with respect to that reserve liability. The third section, reading down, shows a re-estimation of the original reserve shown in the first section. In the third section, the original reserve is re-estimated using information that has become known in subsequent years and as trends become more apparent. The last section compares the latest re-estimate with the original estimate. Conditions and trends that affected development in the past may not necessarily repeat in the future. Accordingly, it may not be appropriate to extrapolate reserve deficiencies or redundancies based on this table.

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Loss and Loss Adjustment Expense Reserve Development

	December 31,										
DOLLARS IN MILLIONS	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Gross Reserve for Unpaid Losses and LAE	$ 541	$ 700	$ 975	$ 1,426	$ 1,511	$ 1,531	$ 1,433	$ 1,323	$ 1,269	$ 1,211	$ 1,119
Deduct:											
Reinsurance Recoverables	36	62	92	325	229	209	138	85	85	77	78
Net Reserve for Unpaid Losses and LAE	$ 505	$ 638	$ 883	$ 1,101	$ 1,282	$ 1,322	$ 1,295	$ 1,238	$ 1,184	$ 1,134	$ 1,041
Cumulative Amount Paid, Net of Reinsurance as of:											
One Year Later	$ 274	$ 341	$ 402	$ 407	$ 487	$ 508	$ 511	$ 518	$ 541	$ 553	
Two Years Later	393	483	531	623	707	742	724	738	757		
Three Years Later	477	521	635	741	830	854	834	854			
Four Years Later	476	570	684	803	891	906	890				
Five Years Later	509	600	715	835	918	943					
Six Years Later	529	619	734	850	940						
Seven Years Later	543	632	745	864							
Eight Years Later	553	640	754								
Nine Years Later	556	646									
Ten Years Later	560										
Reestimate of Net Reserve for Unpaid Losses and LAE as of:											
End of Year	$ 505	$ 638	$ 883	$ 1,101	$ 1,282	$ 1,322	$ 1,295	$ 1,238	$ 1,184	$ 1,134	$ 1,041
One Year Later	564	720	886	1,062	1,190	1,230	1,195	1,159	1,103	1,109	
Two Years Later	612	722	879	1,026	1,131	1,158	1,106	1,088	1,086		
Three Years Later	619	724	872	1,006	1,088	1,106	1,054	1,073			
Four Years Later	623	725	857	980	1,049	1,068	1,044				
Five Years Later	624	719	840	951	1,033	1,068					
Six Years Later	623	709	819	947	1,040						
Seven Years Later	618	693	820	950							
Eight Years Later	608	694	824								
Nine Years Later	609	701									
Ten Years Later	613										

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Loss and Loss Adjustment Expense Reserve Development

	December 31,										
DOLLARS IN MILLIONS	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
Initial Net Reserve for Unpaid Losses and LAE in Excess Of (Less Than) Reestimated Net Reserve for Unpaid Losses and LAE:											
Amount of Reestimate	$ (108)	$ (63)	$ 59	$ 151	$ 242	$ 254	$ 251	$ 165	$ 98	$ 25	
Reestimate as a Percentage of Initial Net Reserve for Unpaid Losses and LAE	(21.4)%	(9.9)%	6.7%	13.7%	18.9%	19.2%	19.4%	13.3%	8.3%	2.2%	
Latest Reestimate of:											
Gross Reserve for Unpaid Losses and LAE	$ 713	$ 800	$ 920	$ 1,276	$ 1,283	$ 1,308	$ 1,193	$ 1,147	$ 1,144	$ 1,169	
Recoverable for Reinsurance	100	99	96	326	243	240	149	74	58	60	
Net Reserve for Unpaid Losses and LAE	$ 613	$ 701	$ 824	$ 950	$ 1,040	$ 1,068	$ 1,044	$ 1,073	$ 1,086	$ 1,109	
Cumulative (Increase) Decrease to Reestimation of Gross Reserve for Unpaid Losses and LAE:	$ (172)	$ (100)	$ 55	$ 150	$ 228	$ 223	$ 240	$ 176	$ 125	$ 42	

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The Company acquired Valley Group Inc. and its subsidiaries (VGI) in 1999. Under the agreement governing the acquisition of VGI, the Company was entitled to recover from the seller 90% of the unfavorable development of VGI s pre-acquisition loss and LAE reserves, subject to a maximum recovery of $50 million. Reserve development shown in the preceding table for the years 2000 to 2004 is net of changes in the Company s estimated recovery, which was received in 2004. Reserves increased in 2002 and 2003 partly due to the Company s acquisition of the personal lines business of Lumbermens. At the end of 2002, the Company also acquired two insurance companies from SCOR. Reinsurance recoverable in 2003 and forward includes a recoverable from a subsidiary of SCOR under an indemnity reinsurance agreement whereby the subsidiary assumed the pre-acquisition liabilities of the two insurance companies acquired by the Company. In 2005, three major hurricanes that significantly impacted the Company (Katrina, Rita and Wilma) made landfall in the United States. Accordingly, reserves at December 31, 2005 increased as claims from these hurricanes were established for adjudication and declined in subsequent years as claims were paid. The Company acquired Merastar Insurance Company (Merastar) in 2007. Accordingly, reserves for this business are included in the table for 2007 and forward. In 2008, three major hurricanes that significantly impacted the Company (Dolly, Gustav and Ike) made landfall in the United States. Accordingly, reserves at December 31, 2008 increased as claims from these hurricanes were established for adjudication and declined in subsequent years as claims were paid. The Company acquired Direct Response Corporation and its subsidiaries (Direct Response) in 2009. Accordingly, reserves for this business are included in the table for 2009 and forward.

Reserve estimates increase or decrease as more information becomes known about individual claims and as changes in conditions and claims trends become more apparent. In 2010, the Company reduced Property and Casualty Insurance Reserves by $24.9 million to recognize favorable development of losses and LAE from prior accident years. Personal lines insurance losses and LAE reserves developed favorably by $21.6 million and commercial lines, including discontinued operations, developed favorably by $3.3 million. Personal insurance losses and LAE developed favorably in 2010 due primarily to the emergence of more favorable loss trends for the 2009, 2007 and 2006 accident years, partially offset by adverse development on certain hurricanes.

In 2009, the Company reduced Property and Casualty Insurance Reserves by $80.9 million to recognize favorable development of losses and LAE from prior accident years. Personal lines insurance losses and LAE reserves developed favorably by $72.3 million and commercial lines, including discontinued operations, developed favorably by $8.6 million. Personal insurance losses and LAE developed favorably in 2009 due primarily to the emergence of more favorable loss trends for the 2007, 2006 and 2005 accident years due to improvements in the Company s claims handling procedures and favorable development on catastrophes.

In 2008, the Company reduced Property and Casualty Insurance Reserves by $79.3 million to recognize favorable development of losses and LAE from prior accident years. Personal lines insurance losses and LAE reserves developed favorably by $45.8 million and commercial lines insurance losses and LAE reserves developed favorably by $33.5 million in 2008. Personal lines insurance losses and LAE reserves developed favorably in 2008 due primarily to the emergence of more favorable loss trends than expected for the 2006 and 2005 accident years due to the improvements in the Company s claims handling procedures, partially offset by adverse development of $8.9 million related to certain re-opened claims from Hurricane Rita, which occurred in the 2005 accident year. Commercial lines insurance losses and LAE reserves developed favorably in 2008 primarily in the Company s discontinued operations. During the fourth quarter of 2008, the Company s actuaries conducted their regular reserve review of the Unitrin Business Insurance run-off business for all traditional reserving groups. In addition, the Company s actuaries updated certain analyses using the Company s experience as well as more recent industry studies to re-estimate asbestos, environmental liabilities and construction defect liabilities. These updated analyses, along with the actuaries regular reserve reviews during 2008, resulted in favorable reserve development of $29.7 million in 2008.

In 2007, the Company reduced Property and Casualty Insurance Reserves by $101.1 million to record favorable development of losses and LAE from prior accident years. Personal lines insurance losses and LAE and commercial lines insurance losses and LAE developed favorably by $44.4 million and $56.7 million, respectively, in 2007. The reserve reductions were primarily due to the emergence of more favorable loss trends than expected for the 2006, 2005 and 2004 accident years, partially due to the improvements in the Company s claims handling procedures.

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In 2006, the Company reduced Property and Casualty Insurance Reserves by $91.6 million to record favorable development of losses and LAE from prior accident years. Personal lines insurance losses and LAE and commercial lines insurance losses and LAE developed favorably by $63.6 million and $28.0 million, respectively, in 2006. The reserve reductions were primarily due to the emergence of more favorable loss trends than expected for the 2005 and 2004 accident years, partially due to the improvements in the Company s claims handling procedures.

In 2005, the Company reduced Property and Casualty Insurance Reserves by $92.1 million to record favorable development of losses and LAE from prior accident years. Personal lines insurance losses and LAE and commercial lines insurance losses and LAE developed favorably by $73.1 million and $19.0 million, respectively, in 2005. The reserve reductions were primarily due to the emergence of more favorable loss trends than expected for the 2004 and 2003 accident years, partially due to improvements in the Company s claims handling procedures.

In 2004, the Company reduced Property and Casualty Insurance Reserves by $39.0 million to record favorable development of losses and LAE from prior accident years. Personal lines insurance losses and LAE and commercial lines insurance losses and LAE developed favorably by $29.7 million and $9.3 million, respectively, in 2004. The reserve reductions were primarily due to favorable development of the 2003 accident year.

During 2001 and 2002, the Company increased Property and Casualty Insurance Reserves to reflect adverse development due to developing loss trends primarily related to construction defect, mold, automobile liability and product liability loss exposures in its commercial lines of business as well as personal automobile liability.

The Company does not discount reserves. There are no significant differences between the Company s property and casualty reserves carried on a statutory basis and those computed in accordance with accounting principles generally accepted in the United States of America, except that such reserves for statutory reporting purposes are reported net of reinsurance in the statutory financial statements.

Catastrophe Losses

Catastrophes and storms are inherent risks of the property and casualty insurance business. These catastrophic events and natural disasters include, without limitation, hurricanes, tornadoes, earthquakes, hailstorms, wildfires, high winds and winter storms. Such events result in insured losses that are, and will continue to be, a material factor in the results of operations and financial position of Unitrin s property and casualty insurance companies. Further, because the level of insured losses that could occur in any one year cannot be accurately predicted, these losses contribute to material year-to-year fluctuations in the results of the operations and financial position of these companies. Specific types of catastrophic events are more likely to occur at certain times within the year than others. This factor adds an element of seasonality to property and casualty insurance claims. The occurrence and severity of catastrophic events are difficult to accurately predict in any year. However, some geographic locations are more susceptible to these events than others. The Company has endeavored to manage its direct insurance exposures in certain regions that are prone to naturally occurring catastrophic events through a combination of geographic diversification, restrictions on the amount and location of new business production in such regions, and reinsurance. The Company has adopted the industry-wide catastrophe classifications of storms and other events promulgated by Insurance Services Office, Inc. (ISO) to track and report losses related to catastrophes. ISO classifies a disaster as a catastrophe when the event causes $25 million or more in direct losses to property and affects a significant number of policyholders and insurers. ISO-classified catastrophes are assigned a unique serial number recognized throughout the insurance industry. The discussions throughout this 2010 Annual Report utilize ISO s definition of catastrophes.

The process of estimating and establishing reserves for catastrophe losses is inherently uncertain and the actual ultimate cost of a claim, net of reinsurance recoveries, may vary materially from the estimated amount reserved. See Note 22, Catastrophe Reinsurance, to the Consolidated Financial Statements for a discussion of the factors that influence the process of estimating and establishing reserves for catastrophes.

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Reinsurance

The Company manages its exposure to catastrophes and other natural disasters through a combination of geographical diversification, restrictions on the amount and location of new business production in certain regions, and reinsurance. To limit its exposures to catastrophic events, the Company maintains various primary catastrophe reinsurance programs for its property and casualty insurance businesses. Coverage for each primary catastrophe reinsurance program is provided in various layers. In addition to these programs, the Kemper segment purchases reinsurance for catastrophes losses in North Carolina at retentions lower than the Kemper s primary catastrophe reinsurance programs. The Company also purchases reinsurance from the Florida Hurricane Catastrophe Fund (the FHCF) for hurricane losses in Florida at retentions lower than those described below for the Company s primary catastrophe reinsurance programs. See Note 22, Catastrophe Reinsurance, to the Consolidated Financial Statements for information pertaining to the Company s primary catastrophe reinsurance programs for 2010, 2009 and 2008. The Company s catastrophe reinsurance programs for 2011 are described below.

Coverage for each catastrophe reinsurance program effective January 1, 2011 is provided in various layers as presented below:

	Catastrophe Losses and LAE		
DOLLARS IN MILLIONS	**In Excess of**	**Up to**	**Percentage of Coverage**
Kemper Segment			
Retained	$	$ 50.0	%
1st Layer of Coverage	50.0	100.0	65.0
2nd Layer of Coverage	100.0	200.0	95.0
3rd Layer of Coverage	200.0	350.0	90.0
Unitrin Direct and Unitrin Specialty Segments			
Retained	$	$ 3.0	%